

NOTICE: Summary decisions issued by the Appeals Court pursuant to its rule 1:28, as amended by 73 Mass. App. Ct. 1001 (2009), are primarily directed to the parties and, therefore, may not fully address the facts of the case or the panel's decisional rationale. Moreover, such decisions are not circulated to the entire court and, therefore, represent only the views of the panel that decided the case. A summary decision pursuant to rule 1:28 issued after February 25, 2008, may be cited for its persuasive value but, because of the limitations noted above, not as binding precedent. See Chace v. Curran, 71 Mass. App. Ct. 258, 260 n.4 (2008).

COMMONWEALTH OF MASSACHUSETTS

APPEALS COURT

18-P-1200

COGNITION FINANCIAL CORPORATION

vs.

COMMISSIONER OF REVENUE.

MEMORANDUM AND ORDER PURSUANT TO RULE 1:28

The plaintiff, Cognition Financial Corporation (Cognition), appeals from a judgment dismissing its complaint for declaratory relief without prejudice. Because we conclude that Cognition's complaint does not present an actual controversy, we affirm.

1. Background. As alleged in Cognition's complaint, Cognition sold its subsidiary, NC Residuals Owners Trust (NCROT), to VCG Owners Trust, effective March 31, 2009. In connection with that sale, Cognition entered into an indemnification agreement whereby Cognition agreed to indemnify VCG Owners Trust and VCG Owners Trust's parent company (collectively, VCG) for any losses incurred due to NCROT's failure to pay taxes owed. The indemnification agreement further provided that Cognition would control the defense of any

claim made by a "Tax Authority" that could result in an indemnity payment under the agreement.

On August 6, 2013, the Department of Revenue (department) gave notice to NCROT of tax assessments, plus interest and penalties, for the periods ending June 30, 2008 and March 31, 2009.¹ NCROT filed a petition for abatement with the Appellate Tax Board, and Cognition is controlling the challenge in those proceedings pursuant to its authority under the indemnification agreement. During the abatement proceedings, the Commissioner of Revenue took the position that the department is a third-party beneficiary of the indemnification agreement and that, pursuant to that agreement, Cognition is directly liable to the department for any taxes owed by NCROT. Cognition disagrees. While Cognition does not dispute that it must indemnify VCG for any losses incurred due to NCROT's failure to pay taxes owed, Cognition contends that it has no obligation to pay those taxes directly to the department. Cognition thus filed this action seeking a declaratory judgment that it is not directly liable to the department for any taxes owed by NCROT.²

¹ NCROT was known as Gate Holdings, Inc. prior to the sale to VCG Owners Trust and is thus referred to as Gate Holdings, Inc. in the tax assessments. For ease of reference, we refer to Gate Holdings, Inc. by its current name, NCROT.

² At the request of the parties, the abatement proceedings have been stayed pending the outcome of this appeal.

2. Discussion. The primary issue on appeal is whether Cognition's request for declaratory relief presents an actual controversy between Cognition and the Commissioner, as required by the declaratory judgment statute. See G. L. c. 231A, § 1 (Superior Court "may on appropriate proceedings make binding declarations of right, duty, status, and other legal relations sought thereby, either before or after a breach or violation thereof has occurred in any case in which an actual controversy has arisen . . ."). The Commissioner contends that there is no actual controversy yet, as there are multiple contingencies that may result in the department not seeking payment directly from Cognition. In particular, the Commissioner notes that NCROT's tax liability remains unresolved and that NCROT ultimately may not owe any taxes. Cognition counters that in the insurance context, an indemnifying party may seek declaratory relief to determine its duty to indemnify even if the indemnified party's liability remains unresolved in underlying litigation. We agree with the Commissioner.

The declaratory judgment statute is "concerned with the resolution of real, not hypothetical controversies; the declaration issued is intended to have an immediate impact on the rights of the parties." Massachusetts Ass'n of Indep. Agents & Brokers, Inc. v. Commissioner of Ins., 373 Mass. 290, 292 (1977). While a party need not "incur the risk of violating

some term of a contract or of invading some right of the other before seeking a declaratory judgment," a complaint for declaratory relief must set forth a real dispute, with "the circumstances attending the dispute plainly indicat[ing] that unless the matter is adjusted such antagonistic claims will almost immediately and inevitably lead to litigation." School Comm. of Cambridge v. Superintendent of Sch. of Cambridge, 320 Mass. 516, 518 (1946). Applying these principles, actual controversies have been found where the parties to a contract are at a crossroads and need their rights and responsibilities resolved to determine whether they may proceed in a certain way. See, e.g., School Comm. of Greenfield v. Greenfield Educ. Ass'n, 385 Mass. 70, 74 (1982) (whether plaintiff could immediately fire employees); Massachusetts Home Mtge. Fin. Agency v. New England Merchants Nat'l Bank of Boston, 376 Mass. 669, 675-676 (1978) (whether defendant was obligated to purchase certain notes then being offered); Carlton Hotel, Inc. v. Abrams, 322 Mass. 201, 202-203 (1948) (whether plaintiff had to pay bill already due).

Unlike in the cases cited, the disagreement here is purely hypothetical. While Cognition and the Commissioner disagree about the effect of the language in the indemnification agreement, a declaration resolving their disagreement would not have an immediate impact on the rights of either party. A

decision that Cognition is directly liable to the department would not require Cognition to pay anything to the department, as NCROT's tax liability has not yet been determined. Nor would the contrary decision end the underlying tax dispute, as NCROT would still be liable for any taxes ultimately owed. In other words, regardless of the outcome of this declaratory judgment action, the abatement proceedings will continue before the Appellate Tax Board.³ Contrast DiStefano v. Commissioner of

³ Cognition suggested at oral argument that the requested declaration could perhaps affect its settlement position and possibly even result in a decision by Cognition to stop defending against the tax claims. Where Cognition does not dispute that it must indemnify VCG for any losses incurred due to NCROT's failure to pay taxes, however, it is unclear why the requested declaration would have this effect.

Moreover, Cognition's suggestion raises another problem in that G. L. c. 231A, § 8, requires that "all persons shall be made parties who have or claim any interest which would be affected by the declaration." Cognition's settlement position and decision whether to defend against the tax claims may affect VCG, which is not a party to this action. The very declaration that Cognition seeks further highlights this problem. As worded in Cognition's complaint, Cognition seeks a declaration that "Cognition has no contractual obligation under the [i]ndemnification [a]greement, and no other legal obligation, to pay taxes, interest, penalties, or other amounts arising from the [tax assessments]." This requested declaration, so worded, could be construed as determining Cognition's duty to indemnify VCG. While Cognition asserts that it intended the requested declaration to limit only the department's ability to demand payment from Cognition, and not VCG's ability to do so, the fact that Cognition's requested declaration fails to accomplish that goal highlights the problem with excluding VCG from this case. Nonetheless, due to our disposition of this appeal, we need not address the argument that VCG is a necessary party, and we decline to do so where the effect on VCG has not been fully developed by either party.

Revenue, 394 Mass. 315, 319-321 (1985) (declaration that taxpayers were not subject to tax ended assessment and abatement process). If the Appellate Tax Board denies NCROT's petition for an abatement of the taxes, numerous other contingencies would still have to come to pass before the department would seek payment directly from Cognition. Only then would this case present an actual controversy.

Cognition's reliance on insurance cases does not persuade us otherwise. Insurance contracts often include a duty to defend that is broader than the duty to indemnify. When an insurer seeks declaratory relief before the insured's liability has been determined, the insurer is doing so to determine its duty to defend, not its duty to indemnify. See, e.g., Improved Mach., Inc. v. Merchants Mut. Ins. Co., 349 Mass. 461, 464 (1965); Dorchester Mut. Fire Ins. Co. v. First Kostas Corp., 49 Mass. App. Ct. 651, 655-656 (2000); Frohberg v. Merrimack Mut. Fire Ins. Co., 34 Mass. App. Ct. 462, 463 (1993). The declaration thus has an immediate consequence: the insurer will either continue defending the insured or not. While Cognition notes that Frohberg, supra at 465, also includes a determination that the insurer did not have a duty to indemnify, that conclusion must be viewed in context. In Frohberg, the insurer's duty to defend turned on the insurer's duty to

indemnify.⁴ Nothing in Frohberg stands for the proposition that it would have been appropriate for us to determine the insurer's duty to indemnify in the absence of a disagreement regarding the insurer's duty to defend. Contrast Newell-Blais Post #443, Veterans of Foreign Wars of the U.S., Inc. v. Shelby Mut. Ins. Co., 396 Mass. 633, 638 (1986) (where insurer had duty to defend but where "the obligation to indemnify does not ineluctably follow from the duty to defend," deleting as premature that portion of judgment declaring that insurer also had duty to indemnify).

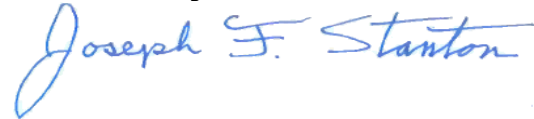
Unlike an insurer trying to determine whether it must continue defending an insured, Cognition seeks a declaration that it is not directly liable to the department for NCROT's as yet undetermined tax liability. Even if Cognition were to receive the requested declaration, Cognition would still control the defense of the underlying tax claims in the ongoing abatement proceedings. Because the requested declaration would not have an immediate impact on the rights of either Cognition

⁴ As we noted in Frohberg, "[A]n insurer has only an 'obligation to indemnify the insured against judgments obtained against it within the policy coverage' and no duty to defend if the underlying complaint does not demonstrate the 'possibility that the liability claim falls within the insurance coverage.'" Frohberg, 34 Mass. App. Ct. at 464, quoting Sterilite Corp. v. Continental Cas. Co., 17 Mass. App. Ct. 316, 318 n.4, 319 (1983).

or the Commissioner, we conclude that Cognition's request for declaratory relief does not present an actual controversy.

Judgment dismissing action
without prejudice affirmed.

By the Court (Blake, Henry &
McDonough, JJ.⁵),



Clerk

Entered: June 26, 2019.

⁵ The panelists are listed in order of seniority.